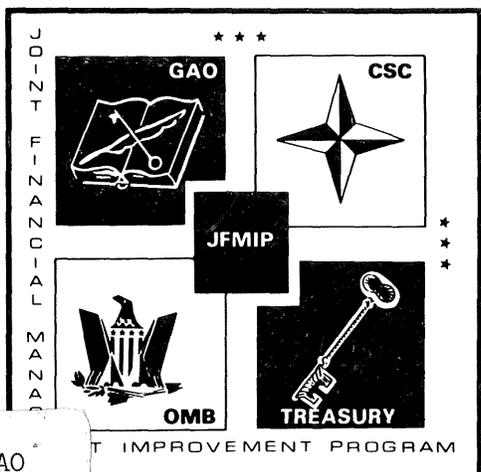


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EDITOR'S NOTES

This document is a compilation of the principal addresses presented at the Financial Management Conference held on February 7, 1977. Opinions and beliefs expressed in this document are those of the authors and do not necessarily reflect the views or policies of the Federal Government or the agencies of the authors.

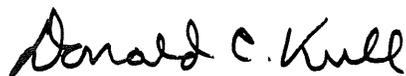
FOREWORD

The Joint Financial Management Improvement Program is a cooperative undertaking of the Office of Management and Budget, the General Accounting Office, the Treasury Department, and the Civil Service Commission, working with each other and with operating agencies to improve financial management on a government-wide scale and in individual agencies. The JFMIP was initiated in 1948 by the Secretary of the Treasury, the Director of the Bureau of the Budget and the Comptroller General, and was given a statutory basis in the Budget and Accounting Procedures Act of 1950.

The Sixth Annual Financial Management Conference was held in Washington, DC., on February 7, 1977. The conference theme, "New Challenges for Financial Managers," was addressed by speakers from Federal, State and local government and the accounting profession. Several topics of current interest were discussed in concurrent workshops.

A special feature of the conference was presentation of the Annual Financial Management Improvement Awards to Alice M. Rivlin, Director of the Congressional Budget Office, and Joseph T. Davis, Assistant Commissioner (Administration) with the Internal Revenue Service.

The principal presentations at the conference are being published in the hope they will be helpful to the conference participants and others who are interested in the improvement of public financial management.



Donald C. Kull
Executive Director

June 1977

DEBORAH KELLY
DIRECTOR OF FINANCIAL COMMUNICATIONS
OFFICE OF THE DEPUTY MAYOR FOR FINANCE
NEW YORK CITY

If ever there was a challenge to financial managers, it is embodied in New York City's fiscal crisis. It isn't so surprising, really, that the "big apple" should be first to encounter substantial and complex financial problems, since New York is not only one of the largest and most diverse cities in the world, but it has an operating budget at just over \$13 billion in fiscal year 1977 and just under \$13 billion in fiscal year 1978, which is larger than either the States of New York or California--in fact the largest budget of any governmental unit in the United States except for that of the Federal Government itself. Clearly New York City has had to come to grips with the overwhelming task of getting its house in order. This task--formidable under normal circumstances--has been rendered herculean as a result of the City's being denied access to the public credit markets. City fiscal management has been placed temporarily under the partial control and supervision of both the State and the Federal Government--through the State Emergency Financial Control Board, and through the Department of Treasury. Among other things, city management is having to construct completely new procedures for financial planning, control, accounting, accountability, reporting, and disclosure.

I am certain you are all familiar with the story of how the "big apple was blighted," but let me review some of the significant events leading up to New York City's financial "crisis" which will provide background for appreciating the revolutionary nature of the financial solutions the City is attempting to execute.

There have been several specific points of "crisis," but the first dates back to the Spring of 1975, when the City of New York was no longer able to market its debt.

For many years, the City of New York had been a large-scale and frequent borrower in the public markets. The City had the largest budget of all American State and local governments and, not surprisingly, it also was the most active tax-exempt borrower. It borrowed for conventional municipal purposes--on a long-term basis to finance capital projects, and on a short-term basis mainly to bridge the seasonal difference between the flow of tax receipts and expenditures, occasionally to cover, temporarily,

year-end shortfalls in revenue, and to provide initial financing of capital projects to be permanently financed later by longer term bonds.

However, for several years prior to 1975, the City had also used short-term borrowing to meet its annual budget deficits and to repay the borrowing of previous years.

The underlying problem was similar in nature to that of many other cities in the United States. During the 1960's, there was a continuous growth of new social programs coming out of Washington and Albany; the City seized upon these in order to obtain maximum financial aid from the other levels of government. But one real effect was to increase City payrolls and expenses, and eventually to contribute to the fiscal problem, when State and Federal aid did not continue to increase at the rapid rates of the 1960's. In the 1970's, New York City experienced a growing gap between a static or declining tax base, and escalating demands and costs for municipal services--the City was increasingly living beyond its means.

In addition, the City of New York bears certain fiscal responsibilities which are not shared by other major American cities. For example, because the City of New York is the exclusive local government for taxing and spending, it must also provide many public services which in other cities are provided by local governments other than the municipalities themselves. In addition, the City historically has provided some public services which are not provided by most local governments in this country, notably extensive hospital and higher education systems. And, unlike most States, New York State law requires the City of New York to fund locally a relatively large percentage of certain other costly services, principally welfare and the court system.

In the early 1960's, the City ended most years with cash operating deficits, usually of modest size. A combination of new and higher city taxes, a buoyant economy, and substantial increases in State and Federal aid financed large increases in spending, but without significant deficits, in the latter half of the 1960's. But after 1969, the local economy turned down, State aid increased only modestly, and Federal aid stopped growing with the adoption of revenue sharing in 1972. Expenditures continued to climb rapidly,

although there were sporadic efforts to restrain the increases. Tax rates were increased, but both the depressed condition of the local economy and political considerations kept those increases from matching the increased expenditures. The result was a rapidly increasing cash deficit in the annual expense budgets of the City.

Various techniques to finance these deficits were authorized by the State Legislature and implemented. These techniques were often complex, and dependent upon the peculiarities and permissiveness of the City's accounting procedures. In addition, such techniques were based upon the assumption that the growing City debt was marketable in ever-increasing volume. Among other things, the City borrowed in increasing amounts against accrued, but actually uncollectable, tax revenues; applied the proceeds of long-term debt to make payments pursuant to collective bargaining agreements; and moved payment dates for payrolls and other expenses forward to later fiscal years. The City also shifted many expense items to its capital budget, and used long-term debt to finance such non-capital programs as manpower training and vocational education, and to pay an increasing array of municipal salaries and other recurring expenses. In these and other ways, the City was able to appear to balance each annual budget. But, in fact, such actions were effectively creating permanent additions to the City's outstanding debt. Once on the treadmill, the City had to continue borrowing, in order to pay off previous debts and to finance new deficits. To market this growing debt, both higher interest rates and shorter maturities were required. By the Fall of 1974, the City was experiencing difficulty in selling its notes, even at rising short-term interest rates. During the first few months of 1975, the City was facing increasing short-term borrowing needs, but was barely able to market its debt, and only to and through a few New York City banks, at interest rates as high as 9-1/2 percent. City borrowing reached a peak in the fiscal year ending June 30, 1975, when it borrowed more than \$9 billion, while repaying more than \$8 billion of previously incurred debt. By April 1975, the City found itself no longer able to borrow at any price.

In June 1975, the Municipal Assistance Corporation for the City of New York was established by the New York State Legislature. MAC's two statutory purposes are to assist the City in providing essential services to its inhabitants without interruption, and to instill investor confidence in the debt obligations of the City. To carry out the first purpose, the statute empowers MAC to sell bonds and notes, and to pay or lend to the City, the proceeds of such sales. MAC bonds are secured by State taxes imposed on retail sales within the City, and State stock transfer taxes. To

assist in the restoration of investor confidence, and for the City to qualify for receiving the proceeds of MAC bond and note sales, the MAC Act requires the City to (1) adopt the State Comptroller's uniform system of accounts for municipalities, (2) to phase out its practice of including certain operating expenses in the capital budget, and (3) to reach a balanced budget in fiscal year 1978. The concept underlying this legislation was for MAC to refinance a substantial share of the City's short-term debt, while the City would work toward paring its fiscal condition down to a manageable size--cutting its budget to the core, so to speak.

However, it quickly became clear that the public market was not receptive to this arrangement. It seems as though most investors, particularly outside of New York City, were unable to distinguish MAC bonds secured by State taxes from obligations of the City.

Despite efforts on behalf of the City to devise new programs aimed at reforming spending and management practices of the City, and diligent attempts to sell MAC bonds to finance the City's tremendous cash requirements, by the end of the summer of 1975, it became clear that the solution to the City's fiscal crisis would require some kind of Federal guarantee for obligations of the type issued by MAC. It also became clear that no such support would be forthcoming without the substantial involvement and commitment of the State of New York. As a result, the State Legislature enacted the Financial Emergency Act for the City of New York in September 1975. This Act created the Emergency Financial Control Board and directed the City to prepare a three-year financial plan, subject to review and approval by the Control Board, reflecting a balanced expense budget in fiscal year 1978. In short, the Financial Emergency Act subjected the City's fiscal affairs, traditionally within its home rule powers, to the direct oversight of special agencies of the State.

Now, I must skip over some of the exciting events of the next few months which include the moratorium, recently declared unconstitutional by the State Supreme Court, and the agreement with the City pension funds to purchase long-term city bonds, and move on to December 1975, when President Ford signed into law the New York City Seasonal Financing Act of 1975. Acting under this law, on December 30, 1975, the State, the City, the Control Board, and the Federal Government signed a credit agreement, under

which the Secretary of the Treasury agreed under the certain conditions to make short-term loans to the City. Of course, there have been many other significant events, but at the risk of being accused of cherry-picking, I have chosen only those which are the seeds for the City's current and future financial accounting and reporting systems. To understand where we are and where we are going in this regard, first, let's examine the legislative requirements for the City's financial systems:

1. The MAC Act required the City to reform its accounting and budgeting methods to bring them into conformance with the State Comptroller's uniform system of accounts for municipalities, as modified by consultation with the City to meet its unique needs. The MAC Act also required the City to design and implement a new accounting system which, by July 1, 1977, would establish records and controls adequate to enable an auditor to perform an annual audit and render an opinion thereon. Furthermore, it required that an audit of the City's annual statements be performed for fiscal year 1978, by the State Comptroller, or at his election, by an independent certified public accountant.
2. The Financial Emergency Act, which created the Emergency Financial Control Board, required that the Board monitor the City through a three-year financial plan, and review the City's operations, managerial efficiency, and productivity. The City is thus required to provide the Emergency Financial Control Board with appropriate reports on its operations and financial activities. In particular, the City provides the Emergency Financial Control Board with proposed revisions to the financial plan for approval.
3. The Credit Agreement providing for seasonal loans required, among other things, that the City provide the Treasury with a monthly statement of the results of operations of the City for the most recent month and year-to-date. The format of the monthly Treasury report was designed by Arthur Andersen and includes: (1) individual reports of the financial plan,

actual performance against the plan, and City forecasts--a best estimate--for the year; (2) cash flow statements; (3) detailed reports of revenue, expenditures, State and Federal receivables, and debt service. The Treasury reports also include a brief narrative analysis of significant changes from the prior month report and appropriate footnotes.

In addition to these requirements which were a direct result of the City's financial crisis, the New City Charter Revision, approved by the voters in 1975, required the following reforms to the City's financial systems: changes in accounting procedures which, in the main, are similar to the changes required by the MAC Act; more thorough review and evaluation of the budget prior to final approval and adoption; quarterly budget allotments; agency budgeting flexibility; decentralization to City agencies of day-to-day responsibility for financial management; and eventually, "geographic budgeting" through which each community district would know what portion of the expense budget is assigned to it.

Beyond these legislated requirements for reform of the City's financial procedures, the City clearly must regain access to the public credit markets in order to become self-supporting again, given its tremendous short-term and seasonal cash requirements as well as longer term capital needs. Obviously, balancing the budget is the necessary first step and City officials are confident that this can be achieved in fiscal year 1978. However, on this foundation the City must build a sturdy structure of responsible, professional, and accountable management policies and procedures. The burden of proof rests on the City to convince the public that the budget will continue to balance in future years. This demonstration requires a reporting system which serves both the internal management function and the external disclosure requirements of the public and potential investor. Such a dual reporting system is quite common in the private sector, but relatively new ground for a municipality or any government unit for that matter.

City management has accepted the challenge of building such a system and the effort is well underway. We recognize that this system will serve as a benchmark for others and a basis for future systems. The project has required the cooperation of independently elected officials, professional consultants

and the dedicated efforts of hundreds of City employees, supplemented by experts contributed by business in the City. The project has been christened IFMS, which stands for Integrated Financial Management System. The task of implementing the IFMS project was begun in January 1976 when the Mayor delegated responsibility for the project to the Deputy Mayor for Finance at that time, Kenneth Axelson, currently John C. Burton. The IFMS project is a managerial initiative on the part of the City in response to the legislative requirements of the MAC Act, the Financial Emergency Act, the New York Seasonal Financing Act of 1975, and the New City Charter. All of these coincident requirements for changes in the City's financial practices were viewed by the City as an opportunity to undertake a comprehensive review of its financial systems and operations rather than make piecemeal changes. The scope of IFMS and its impact on the City are thus considerable.

The basic objectives of the new system are as follows:

1. To facilitate improved financial management of the City's resources by agency;
2. To exercise sound budgetary and accounting control over City revenue and expenses; and
3. To accurately report financial information to City managers, Federal and State officials, the investment community, and the general public.

To achieve these objectives IFMS will contain four major subsystems: budgeting, accounting, payroll and purchasing.

The principal functions of these subsystems will include:

FOR BUDGETING

- allocating funds to city agencies and their organizational subdivisions,
- accumulating estimates of revenues to be earned by the City from approximately one thousand separate sources, and
- controlling spending and monitoring revenue collection during the year.

FOR ACCOUNTING AND FINANCIAL REPORTING

- providing a standard method for recording all financial transactions,
- summarizing and reporting the City's financial transactions and financial status for use by agency heads, the City Administration and the financial investing public, and
- comparing and controlling actual expenditures against the budgeting, payroll, and purchasing subsystems.

FOR PAYROLL

- controlling new appointments, paying City employees and accounting for these payments.

AND FINALLY, FOR PURCHASING (ENCUMBRANCE CONTROL)

- expediting the process of obtaining goods and services needed to conduct the City's business, and ensuring that spending limits are observed while providing adequate accountability over the expenditure of funds.

In the past, the Mayor prepared the budget according to one accounting system and the Comptroller paid the bills according to a different system. The result was often inconsistent numbers and inconsistent reports. IFMS will eliminate the inconsistencies because all of the City's financial systems--budgeting, accounting, control, and reporting--will be integrated into a single system, with one data base, supported by a single, centralized data processing facility, the Financial Information Services Agency (FISA). FISA will manage functions newly centralized under IFMS: computer center operations, systems support and data base administration.

The City's new budgeting subsystem will be based on the concept of "responsibility budgeting." Specific managers will be made responsible for every revenue and expense item in the budget. For example, the operating or expense budget will be formulated and controlled on an organizational basis, with every dollar budgeted clearly within a manager's "responsibility center." Agency managers will know what their spending and personnel ceilings are and will be given the informational tools to ensure that they stay within those limits. There will be a detailed revenue budget in which the specific organizational unit responsible for earning and collecting the revenue from each source is explicitly shown.

In accordance with the revised charter, the new purchasing subsystem will delegate detailed pre-audit responsibilities to agency managers. IFMS will impose strict discipline on an agency manager in that no commitment will be possible unless there are sufficient funds available in the manager's budget.

The new payroll subsystem will be integrated with the budgeting and accounting subsystem thereby allowing automatic entry of payroll charges directly into the accounting subsystem and permitting more stringent budgetary control over payroll actions.

The accounting and financial reporting subsystem will contain reporting capabilities to help managers keep track of revenues and expenditures, identify potential problems, and develop plans for the future. Among the reporting capabilities will be monthly reports showing actual expenditures, revenue earning and cash collections compared to planned amounts, reports on budget modifications, personnel reports and purchasing control reports.

The target date for implementing the essential features of IFMS is July 1, 1977, and the project is substantially on schedule at this time.

With the IFMS system providing the basic information resource, the City can embark on the development of a comprehensive public reporting system which might include: monthly financial reports, such as those currently submitted to the treasury; quarterly financial reports reviewed, but not audited by an independent public accountant and certified by the Mayor and the Comptroller; annual audited financial statements prepared on the basis of generally accepted accounting principles for municipal governments, and including a narrative analysis of principles applied and variances contained within the statement; and an additional annual reporting of the economic condition of the City and performance analysis of various programs and services--a kind of evaluation which goes beyond financial statements alone.

It is significant to note that on September 30, 1976, the City issued its financial statements for the fiscal year ending June 1976. This marked the first time in its history that the City published annual financial statements. These statements, prepared to the extent possible, in accordance with generally accepted accounting principles for municipalities, represent the first phase of the City's intense effort to produce audited financial statements in fiscal year 1978.

We, in the City, recognize the difficulty and profound importance of this undertaking. We realize the need for responsible and professional management in government. And we are committed to restoring the City of New York, the big apple--to the preeminent position of first, and best of cities--in fiscal health as in theater, art, fashion, finance, and ideas.

DALE R. McOMBER
ASSISTANT DIRECTOR FOR BUDGET REVIEW
OFFICE OF MANAGEMENT AND BUDGET

The word "challenges" (in the Conference Theme, "New Challenges for Financial Managers") is a substitute for the word "problems." That doesn't mean I don't use the word "challenge." As a matter of fact, during the last two weeks, I find myself no longer talking about the problem of balancing the budget in 1981; I talk about the challenge of balancing the budget in 1981.

Challenge, of course, is upbeat. It is forward looking. It implies constructive effort. Problem is a word that is accompanied by a sigh. As we look around us in the financial management area in the Federal Government these days, it is difficult to avoid a few sighs. There are problems and challenges for all of us. Indeed there are even a few dilemmas thrown in.

Now this is not to say that the problems of financial management, Federal financial management, in the late 1970s are greater than those of other times. Back in the late 1940s and early 1950s when the JFMIP was incubated, I suspect that those who were concerned with financial management felt beleaguered by the difficulties of making immense changes in the creaky Federal financial system when the government was becoming increasingly complex.

Perhaps it is because I am getting old and idealistic about the past, but I have a distinct impression that approaches were a little different in that time of challenge than they are now. When Messrs. Freese of GAO, Calkins of Treasury, and Holchster and Tiller of the Bureau of the Budget sought a new system of accounts and moved toward program budgeting, they must have had differences of opinion, but they must also have had a sense of common goals that overcame those differences. In my imagination, I see them talking to each other directly with enough time to get improvements made, with easy access to the heads of their agencies who, not so incidentally, were very interested in their work. In my imagination, I see them with a comprehension of the whole financial management system of the Federal Government. Above all, I see them as having a clear agreement on what they were trying to accomplish. With their singularity of purpose, the financial managers of the early 1950s got mutual understanding from the Congress and the Executive Branch of the need to simplify the Federal account structure, to move toward program budgeting--notable accomplishments in any age.

Those were simpler times perhaps. In these complex '70s we look to institutions to solve our problems, not personalities.

Before we cite a few of those problems, we might take an irreverent glance at the institutions. There is the General Accounting Office throwing manpower at every suggestion of any conceivable improvement in the Federal establishment anywhere, or at least those that reach the receptive ears of any Congressman.

There is Treasury trying to summarize in a short statement 200 years of fiscal transactions of the powerful and august government of the United States of America in order to show that the largest enterprise in the Western World is about to go down the financial drain.

There is the Civil Service Commission waist deep in a sea of backlogged personnel applications with its attention concentrated on keeping its halo straight.

And then there is OMB, an institution--forgive me for saying it--an institution of which I am proud, but an institution with its head in an ivory tower, its eyes buried in a budget, all the while kicking out paper-producing directives like a chicken kicking in the sand.

Of course it is easy to become cynical in our business. Our little subculture, which is not really very little anymore, has gone through movement after movement aimed to improve us and the larger Federal culture in which we exist--from work measurement and performance budgeting to program budgeting, to cost-based budgeting, to program-planning-budgeting, to management-by-objective, to zero-base budgeting. We continually evolve new rituals for our society. We have gone from CBB to PPB to ZBB, and perhaps in reaching the letter "Z", we have reached the ultimate in our search for answers.

I don't mean to deplore those movements. Goodness gracious, how could we do without them. How could we send our apprentices to symposia and workshops, how could we give our middle managers trips to Monterey or Atlanta or Oak Ridge, what could we old men make speeches about, how could we justify our luncheons and our cocktails, and what in the world would our organizations do for programs. Think of the immense economic loss to all those companies that consult, train, and print brochures. Forgive me for my fun. It is intended to be deliberate. We tend so often to adopt reforms with such serious, almost religious, fervor.

We do indeed need reform. We have seen a major congressional reform in the budget area, and it is working. Congress has found a mechanism to focus on the budget as a whole. The legislature is accepting overall budget responsibility. It has developed sizable staff. Members have become educated in the complexities of the budget mix and budget trends and in macroeconomics.

But with the development of knowledge comes interest. And with the expansion of staffs comes development of concerns. And with the development of concerns comes papers. Each year we can fill a tall filing cabinet with the output of staffs of the Budget Committees, the Congressional Budget Office, and the General Accounting Office that did not exist four years ago.

It is in these areas that we find many of today's challenges for financial management in the Federal Government.

Information and Classification

One of the challenges goes like this: The financial system and budget of the United States is very complex and difficult to understand. What we need is a way of obtaining and classifying information that will reveal to the busy Congressmen what it all means, that will bring enlightenment.

Also, the new budget system requires each committee of the Congress to make its recommendations in the form of figures that will fit into budget resolutions. All of this results in a desire to have data that does not fit the normal Federal account structure. Each committee wants to obtain data tied to its provisions of the law, often below the account level. Each proponent of a classification scheme wants to extract from broad account data that information that fits its own focus. Further, because the Congress uses the budget functional classification to set its targets, that classification has become very meaningful.

All of this has generated a huge variety of suggestions for new information or revised classifications. Both the General Accounting Office and the House Budget Committees have suggested revision of the functional classification. Needless to say, their views are different. OMB has always had considerable difficulty in getting agreement on revisions of the functional classification within the executive branch and even within OMB itself. Now agreement must be reached with appropriate parts of the legislative branch in ways that are not entirely clear in law.

During the past six months, OMB has received two entirely different suggestions for a new classification of research and development programs. I hope I am not revealing too much but those two proposals came from different parts of GAO.

Major agencies are being asked to produce outlay and other data that ties to specific provisions of the law rather than to budget accounts. The volume of materials moving to the Congress grows exponentially.

Perhaps the epitome of the information challenge comes in the zero-based Sunset Bill that last year was designated as S.2925; this year, I understand, it is designated as S.2, perhaps an indication of priority. That Bill would require identification of programs tied to provisions of the law with zero-base reviews of each program specified by committees of Congress. The Senate Rules Committee estimated that several thousand programs would be identified, each generating the need for a discrete set of data.

Along with these desires for data, we have the requirement of Section 601 of the Congressional Budget Act which states that, beginning with the 1979 budget, there is to be included a classification based on agency missions and national needs. This requirement hardly seems to have the enthusiastic support of every part of Congress concerned with such matters, except for, of course, a narrow group that happens to reside in the Senate. Nevertheless, that classification is required by law, and we will obey the law.

Timeliness

At the same time, the Congressional Budget Act has produced the need for more data classified in more ways. The Act has placed greater emphasis on producing data with greater speed and on timeliness.

Our financial culture is driven by the deadline. With the change in the fiscal year, there has been no change in the date for submittal of Treasury's annual statement on the budget. Agency books must now be closed with greater speed and with less time to report to Treasury. The experience of last fall proved that despite help from our improving technology serious problems are caused by this need for speed. It has become increasingly difficult to avoid errors and to keep Treasury accounts data and budget data reconciled.

The push for speed in providing data to meet the demanding schedule of Congress is affecting the day-to-day

work of the accountant and the budgeteer. The annual process flashes by at a frantic pace. Of course it is easy to see the problems created by the Congressional Budget Act. Stated succinctly: How can the legitimate desire of Congress for information be met, and how can we do it in a way that will meet the time schedule?

Other Demands

There are other demands from congressional sources for changes in our system; so let me mention just two. Last year the House Government Operations Committee recommended separate appropriations for ADP operations. The recommendation reflected a legitimate desire for information on this object of Government expenditures. So far, we have resisted that recommendation. Surely we dare not begin to erode the program budgeting principles we established over 25 years ago.

A second kind of demand: As Congress has gained greater understanding of the budget process, members of Congress have begun to learn that control over Federal spending cannot be exercised completely by setting limits on budget authority as traditionally defined; so there are attempts to change the system to maintain greater control. For example, it is being suggested that the concept of public enterprise revolving funds inhibits congressional control and such public enterprise funds should be eliminated.

Zero-Base Budget

And then, of course, there is the zero-base budget. On the one hand we have S.2, the Sunset Zero-Base Budget Bill, that is different in a fundamental way from the zero-base budget system the President plans. The Bill covers a system of congressionally mandated reviews, while the presidential plan covers a system of presidentially mandated budget presentations.

Both the Bill and the President's process call for establishment of program objectives--program objectives articulated on the one hand by committees of Congress, and on the other, by the Executive Branch. They also call, in both instances, for identification of program entities. I don't know whether the Bill will pass or not, but I do know that the Executive Branch will have a zero-base budget system, and we will have it for FY 1979.

That system will include the following: First, comprehensive justification of agency budget proposals in the form of decision packages that separately identify various program levels or options.

Second, a determination during the annual spring planning review process of those programs to be covered by decision packages; that is, to identify what kinds of programs will be covered by decision packages, and, separately, those programs that are to be covered by in-depth reviews.

And, incidentally, if any of you can think of a bright new succinct description or words that we can use to cover those two kinds of things, we would appreciate hearing about it.

Third, a priority ranking of those decision packages at the agency level with participation in that process by all parts of each agency and the use of those results in presidential decisions on the annual budget.

Like all the movements for improvement of the budget aspects of financial management systems, the zero-base budget will place great emphasis on evaluation and quantitative measurement. Once again we are being asked to find better ways to measure program results.

Now we come to the basic challenge that faces us all: How can we devise a system that meets the needs and desires of both the President and the Congress? We might ask ourselves these questions: Can we devise a new system of accounts that will permit derivation of program information however the program might be defined? Can we relate program information to objectives? Can the Executive and the Congress agree on a single set of objectives, and, can we articulate those objectives? Can we reach agreement on a functional classification that both Congress and the Executive can use and that merges the national needs and functional classifications; should the basic account structure of the Federal Government be changed in order to permit Congress greater control over Federal spending? Can we provide the information that is needed to support these systems; and can we do it all without a breakdown in the system?

I don't know how all of these questions will be answered. We are working on some of them. But I think I know that we cannot answer them effectively until we can agree on some first principles, and let me suggest three:

First: Simplicity. Surely we must agree that it is necessary to find ways to make the Federal system a simpler one.

Surely it is the duty of those of us who advise the Congress and the President to suggest simpler ways to finance Government programs and to report on them. Complexity is the enemy of efficiency. As President Carter has said, we must make Government understandable to the people, and that includes members of Congress. It would be quite possible to devise congressional and presidential zero-base systems that could smother us all in paper. We must find a way to avoid that paper. We must find a way to keep it simple.

Second: Communication. Less than thirty years after the founding of our joint program, we have lost the ability to communicate.

We have created special staffs to handle all of our problems, yet somehow we seem able to communicate with each other only in the form of voluminous reports, each of which has a bottom line: "Why don't you do right?" We need to return to the direct discussions which enabled our founders to accomplish so much.

Third: Understanding. With expansion of staffs and with greater complexity, we seemed to have lost the ability to look at the whole financial management system in a comprehensive way.

Each staff with its narrow focus seeks to solve a specific problem to meet a singular need. Where are those people who can look at the whole system and devise integrated comprehensive solutions to our problems?

Well, there they are--the challenges. I suggest that they can only be met by simplicity, communication, and understanding.

WILLIAM R. SNODGRASS
COMPTROLLER OF THE TREASURY
STATE OF TENNESSEE

I think there are some advantages in being last on the program. It has given me an opportunity to hear the trials and tribulations of the City of New York and how they are going about trying to deal with their problems; also, to get some perspective of what the Federal Government is trying to do in dealing with its problems to meet the needs of the executive as well as the legislative branch of the Government.

I could say that we have understood all of those problems at the State level and have met them and could give you the advice you need to solve all of your problems. However, I don't believe I am going to quite do that. I would say, however, that perhaps some of us at the State level are five to ten years ahead of some others in recognizing the problems and trying to find innovative ways of dealing with them because most of the terms that have just been mentioned here, whether they are in vogue at the moment or whether they have been discarded, originated at the State level.

Given the nature and participation at this conference, I should like to consider the challenges we face as governmental financial managers in at least two contexts: First, in context of our individual position responsibilities at our respective levels of government, and secondly, in an intergovernmental context.

I believe we must find that, as public sector financial managers, we have recognized and attempted to address many of the challenges that have confronted us in each context in the recent past, and we have made progress. Nevertheless, we must continue to pursue the many unfinished items on that work program. We face new and changing demands and responsibilities. We must find the way to make progress in response to these as well.

My next observation may be less predictable. I believe that there are aspects of our new concerns that insist that we seek progress in the form of new approaches, techniques and perspectives, but that in the pursuit of such progress and in response to such expectations, it is critically important that we oppose and expose quick fixes,

easy solutions and precipitous actions. We must apply this caution in the way we fulfill our individual responsibilities, and we must exert our collective professional influence to bring such risks to the appropriate attention of governmental policy makers, interest groups, and the public in general.

Initially, let me illustrate this latter concern of mine with a few sketchily drawn examples.

After a number of years in the fiscal management side of State government, I have grown wary of those who suggest that government is just like business, that government should be conducted like a corporation, and that the tools and solutions of the business sector can be indiscriminately applied to the needs and problems of government.

At such times, I hope that we who know government, and also have the necessary technical competence, will be rigorous in our examination of such suggestions and forthright in the enunciation of our findings.

In somewhat related fashion, I prefer to reserve for myself the right of second thoughts regarding newly-minted theoretical solutions in the form of either all-encompassing systems and techniques, or massive new program strategies and structures. This is not intended as a blanket indictment of new ideas and perspectives, but there is a substantial gap between a model in the researcher's computer and the realities of government management. The underestimation of that gap may account for the noticeable decrease in enthusiasm in government management circles for the designation "PPB." Out in the States, many of the component parts of the planning-programming-budgeting concept are functioning in viable and effective fashion, but you may be sure that their proponents make small effort to emphasize their heritage.

Again, I do not intend to speak against change. The progress we must make will have to include new approaches, but we must maintain a healthy constructive criticism in the face of promises of quick, easy answers.

Another variant to this theme is the possibility that in our pursuit at the policy level or other high order objectives and concerns we may unnecessarily constrain or otherwise hamper the conduct of our management

processes, and note that I said unnecessarily. I suspect that each of you in the audience could, after a few moments' consideration, recall such an example.

My colleagues and I in State auditing are currently disturbed by what we feel is such an instance. Congress, in the 1976 Tax Reform Act, took a number of steps to enhance and extend the privacy protection afforded Federal tax information. As most of you know, State tax systems are usually partially built upon, or related to, the Federal income tax structure. For this reason, certain Federal tax information is made available to State tax and revenue agencies, but the provisions of the new law create potential barriers to State government management processes. It would appear that either the State tax functions will not be able to use Federal data for certain necessary control and tax audit tests, or State auditors will be precluded from carrying out their constitutional and statutory audit responsibilities as regards these State agencies.

We believe that there was not necessary conflict between Congress' appropriate concern with protecting the privacy of taxpayer information and the professional conduct of audits of State tax and revenue functions.

Now that I have tried to describe my summary observations that we have been making progress, that we face new challenges that have to be addressed, and that we must be cautious of easy answers and precipitous actions, I'd like to discuss with you some of the factors and my thoughts that lead me to these conclusions. To do this, I would like to touch on where I think we have been and what some of our problems have been; then review some of the areas where I feel significant progress has been made; and then conclude by noting some specific current challenges and what seems to be happening with regard to them.

First, where we have been and the progress made: I think the world of the financial manager in government has been exciting and challenging during the last dozen or so years, and I think it might be useful to review where we were at the beginning of such a time period and what has happened with some of the issues we have had to face.

Looking at State government, there really wasn't a financial management discipline, as we view it today, prior to the turn of the century. The executive budget movement

in State and local governments before and after World War I and the fiscal difficulties associated with the depression of the '30s provide the beginnings of our story. Financial management in that setting centered on fiscal control and was embodied in the movement to create management processes and control functions centralized under the chief executive officer, usually diminishing individual executive agency latitude and also impacting the role of other branches of government.

The financial manager of that day was involved in creating, operating or monitoring fiscal control and stewardship. There was little attention in the government financial management dialogue directed to strategic planning, broad policy choices, measuring program results, the effectiveness of internal management processes and systems, legislative oversight, and broad public disclosure accountability.

In the post-World War II era, everything I have just noted began to change, at least in State government. I should like to quote from Supreme Court Justice Louis D. Brandeis, "It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory and try novel social and economic experiments without risk to the rest of the country."

Not only is that an appropriate and necessary role, but also I believe that in the post-war period the States have been admirably performing in this capacity, and particularly so with regard to financial management.

When I first served as a State budget officer in the early 1950's, our budget process was a bookkeeper's dream. It was a line item, object of expenditure compilation that established to the last detail the authorized expenditure for office supplies, but woe unto anyone who sought to discover the magnitude of the State's total commitment to improved health or services to the disabled.

Since that time, the States have been through performance budgeting, program budgeting, capital budgeting, functional budgeting, PPB, and now zero-base budgeting. We may at times, have been naive in our experimentation, but we have certainly been bold.

Today there are State budget systems that provide budgetary information to decision makers, to agency management during budget execution, and to the instruments of accountability, by fund entity, by program, by formal organization reference, by source of funds, and by activity and by object.

These budget systems are frequently integrated successfully with the State accounting system, and the States have made significant progress in bringing in such previous autonomous functions as highway departments, State university systems, and regulatory boards and commissions. Not all States have progressed at the same pace, but the overall record is impressive. The financial manager cannot guarantee good policy choices, effective operating management or meaningful oversight, but he can and must provide the necessary tools and should exert himself in the policy-making processes.

In the post audit area, the States, even before the Second World War, began to redefine and restructure these critical functions. First, over about a 20-year span, almost all the States redirected the thrust of their audit functions from pre-audit/voucher approval to the performance of true external, post audit reviews, the old pre-audit functions being appropriately reassigned to central accounting. Also at this time, the States moved to establish the necessary structural basis for the audit function's independence. Currently, there are less than one-half dozen States which do not have either a constitutional or statutory legislative auditor or a popularly elected auditor. More recently, we can identify substantial progress in the States to establish effective agency internal audit capabilities as a support component of agency management and an assist to the independent post audit.

In the 1950's, State audit shops moved to expand the scope of their work to include management and systems reviews, and by 1960 States were establishing mandates for full-scope performance and program effectiveness audits. Of particular note is the section of the 1961 Revised Constitution in Michigan which directs the Auditor General to conduct performance audits. The history of response to this change is documented in a volume that is still a useful reference entitled The Performance Post Audit in State Government by Dr. Lennis Knighton, who is now the Legislative Auditor of the State of Utah. As a final indicator of our progress, I am

pleased to report that there is now a growing number of States where every board, agency, commission and department is audited by the independent post auditor on a one, two or three-year cycle. I am particularly pleased that Tennessee has been in this category for several years.

With regard to the State accounting function, perhaps the most necessary challenge has been to move from locating this responsibility in the separate executive branch agencies, each with its own procedures and conception of governmental accounting, and to instead create a uniform statewide accounting system, centrally located. Today perhaps only three States do not have centralized accounting systems. This is a challenge which I would particularly commend to the attention of the Federal Government.

Along with centralization and uniform accounting have come other new developments. We still have at least one State with almost one thousand separate fund entities, but we also have States with fewer than a half dozen accounting fund entities, and I would like to emphasize that I said fund entities and not just fund types. State government financial managers are demonstrating that fiscal integrity, control and stewardship can be maintained through the appropriate use of such mechanisms as restricted accounts without the sacrifices inherent in inflexible and cumbersome excessive fund structures.

In many States these systems are successfully performing multi-purpose roles. I noted earlier that there are examples of State accounting systems successfully integrated with a variety of budgetary practices. In addition, State accounting systems are operating that are responsive to the reporting needs of policy and program management, statutory mandates of stewardship accountability, and also providing a basis for governmental entity, public disclosure, and reporting of financial condition and results of operation. As an important aside to this last point, at least two or three States have, in recent years, experimented with variations of totaled, summary, condensed, or consolidated annual reporting for the entire State government. It might be interesting to compare these efforts with the Federal Consolidated Statement Project to be discussed in one of the workshops this afternoon.

If time permitted, I would also enjoy discussing with you today the challenges and responses in State government in such areas as cash and investment portfolio management, structural reorganization in our executive branches, procurement and property management practices, design and utilization of computerized information systems, innovations in program evaluation, and the dramatic developments in legislative oversight, including our new "sexy" legislation of sunshine and sunset. Time does not permit this. However, I can't conclude this part of my presentation without touching on a point about which I feel very strongly, and that is, long-range fiscal planning and debt management.

I think we are all aware of suggestions that we are in an era of "bad news journalism." I am not particularly interested in participating in that debate, but I do feel that the reporting of the fiscal difficulties of some local or State jurisdictions has not been balanced by a recognition of all the sister State governments and political subdivisions whose fiscal conditions are sound, who find a warm welcome in the market when they choose to issue debt, and who have devoted substantial effort to implementing sound long-term financial practices, including the actuarial funding of retirement systems.

In my own State we are proud of our AAA bond rating and feel that we have made a conscious effort to earn it. If the media were to look at the States more generally, they would have found another, and more positive, record of fiscal management extending back over several decades.

Many States have reduced the ability of individual agencies and semiautonomous entities to independently create long-term obligations and have created strong, effective central review and approval mechanisms for debt. They have acted to abolish or draw down backlogs of unused authorization, and they have managed their outstanding indebtedness and designed their new issues to conform to principles of sound finance.

In addition to those unnoticed local jurisdictions who have similarly chosen the path of responsible fiscal management, there is a long record of State activities providing assistance and guidance to their political subdivisions. It should be pointed out that many State and local governments are already doing an impressive job of responding to the changing expectations regarding the disclosure requirements associated with municipal issuances.

Still, in regard to the problems we've identified in the past, I would like to examine some questions which are more intergovernmental in nature.

In a meeting in this same facility seven years ago, I described an agenda of intergovernmental financial management issues of a then-pressing nature. In part I noted:

"It is well to remember that all Federal grant-in-aid programs are also State programs. They are carried out under legislation enacted by State legislatures, they are administered by State program agencies in the executive department of our State governments, and they are partly controlled by administrative and fiscal controls exercised over all other operations of the State government... Monies received from the Federal Government for carrying out these programs are no different from any other monies received into the State treasury and, therefore, must be subject to the same planning, programming, budgeting, accounting, purchasing, funding, auditing standards and rules that control all other operations of State government.

"I think it is important that we State officials recognize the responsibility for these programs and funds in this manner and that federal officials likewise understand that these programs are also State programs in which they participate.

"The position of the States is not that of a private contractor performing a service for a federal agency where the contract is optional on the part of the private concern and where all terms are dictated by the Federal Government which may be paying all the cost.

"The relationship between the federal and State governments must be one of partnership, and to accomplish this partnership there must be developed an atmosphere of mutual confidence and trust, a condition which has not always prevailed."

As a result of the proliferation of authority in the various agencies for all administrative, financial and procedural requirements, we have seen almost as many sets of written procedures as there are grant programs. Program planners at the Federal and State levels should not have to devote their time and efforts in these areas which are common to all programs. In most States, program departments

have no authority in the determination of overall administrative and fiscal policies and procedures.

What are these areas of administrative and fiscal policy and procedure requirements about which we are speaking? I believe the nineteen broad areas I set forth in my presentation at that time provide a good listing for our purposes. They are as follows: application process; funding policies; funding methods; cash depositories; bonding requirements; grantee personnel and qualifications; compensation; property management; budget revisions; matching funds; program income; financial reporting; closeout procedures; dispositions of unused grant funds; audit; disallowable costs; grantee internal procedures; relationships with subcontractors; and coordination with State and local government requirements.

Seven years ago I described that list as a comprehensive action agenda, and I also attempted to look at the problem from a Federal perspective and noted:

- "1. There are fifty States and a maze of local governments, including 3,000 counties; 18,000 municipalities; 17,000 townships; 35,000 school districts; 1,000 housing and urban districts; 2,200 drainage districts; 2,400 soil conservation districts; 3,200 fire districts; and 700 health and hospital districts. According to this count, there are 92,000 local units of government with which the Federal Government may relate.
- "2. Each State is organized differently with varying responsibilities given to the executive offices of the governor, as opposed to operating agencies, some of which are, in many States, independent of the governor.
- "3. Varying degrees of legislative or legislative staff participation is found to exist in the separate States, sometimes with little coordination with the executive branch of the State government.
- "4. Varying degrees of program coordination and budgetary control exist.

- "5. Varying degrees of financial accounting and internal control systems are to be found.
- "6. Varying degrees of accounting for program and statistical purposes exist.
- "7. Varying degrees of adequacy of audit."

Today one of our questions is, "What have we accomplished in the last seven years?"

From the Federal perspective there are still just as many different units of State and local government, and they still keep going about their responsibilities differently. As I've already suggested, I think that is necessary and healthy. Regarding the other points, I think the States have come a long way. In fact, I think we have come far enough that maybe we are ready to be admitted to partnership in the management of our fiscal affairs in our intergovernmental system.

So, let's turn to the other section of my seven-year-old list and see if the States have moved beyond junior partner status. I said then that from a State viewpoint the next steps should include:

- "1. Through a single staff agency effectuate coordination of federal grants to the state;
- "2. Effectuate grant consolidation at least along functional lines;
- "3. Eliminate organizational requirements from conditions of eligibility;
- "4. Standardize administrative and fiscal policy and procedural requirements common to all grant programs;
- "5. Simplify program requirements, giving greater flexibility and decision making authority to state program agencies where such agencies evidence this responsibility would be justified."

As I examine those five points, I have to conclude that we have taken a shot at each of them and made considerable progress with some. What is the specific track record on which I base this finding? Without elaboration,

I'd note the following: first, the Federal circulars--the A-85 and A-95 processes for regulation and program review; the A-73/FMC 73-2 on audit; the A-102/FMC 74-4 on standard administrative requirements; and the A-87/FMC 74-4 on uniform cost. In addition, such other developments as block grants, revenue sharing, Federal regional councils, waiver of single State agency and separate bank account requirements, letters of credit, and the IGA/joint funding simplification. The list can easily be made longer. Some items listed, and some omitted, have been successful. Others, such as the REGIS-OBIS complex, have had their problems.

Overall, we have made significant progress. Perhaps just as important is the progress we've made in talking to each other: three JFMIP-Council of State Governments Intergovernmental Financial Management Conferences; this 6th Annual JFMIP Conference; the National and Regional Intergovernmental Audit Forums; the annual winter meetings of OMB and the National Association of State Budget Officers, and the activities of ACIR.

There are more, but my point is that over time there may have been a payoff to all the talk. Where does that leave us? Certainly the task is not finished. In fact, even though our old agendas are not complete, new challenges have developed.

I would like to spend the remainder of my time on a few specific questions that are of immediate concern.

Perhaps the most useful way to examine our current agenda of issues is to establish some definition or concepts we ultimately hope to achieve. I would offer the following:

In the States, the kind of past progress I have earlier noted, I hope, will have progressed to a point where critical State management structures and administrative capability would be effective for the States' own needs and, further, could be demonstrated to be also responsive to the needs of the Federal Government regarding Federal assistance programs. Thus, the States would manage Federal concerns in the same way they administer solely State concerns, and the Federal Government would place full reliance upon the States.

On the Federal side, the whole Federal assistance activity would be, I hope, further restructured, duplicative and unique requirements eliminated, and the additional necessary authority or flexibility established to allow Federal managers to, in fact, place reliance upon State systems and responsibilities.

Thus, at the State level, Federal financial resources and program objectives would enter the State system and would thereafter be subject to the system just as though they were State generated resources and State priorities and goals. For Federal managers their concern would be, first, to initially insure the adequacy and reliability of State systems, but accepting that the criteria is system performance, not uniformity; and, secondly, to monitor State practice to determine if they are applying the same standards and controls to Federal interests as to State interests.

If this is a reasonable direction to seek, what are the next steps to get there?

Clearly, we have to continue to address additional attention to items on the old agendas. Some circulars have never been fully implemented; not all Federal regional councils are equally effective. There are still too many separate congressionally created programs and too many Federal agencies and departments that overlap and create unnecessary burdens on everyone because their activity is uncoordinated. That's the Federal side. What about the States?

I've argued earlier that we've made very real progress, but not all the necessary conditions have received equal attention, and not all States have moved at the same pace. Let me suggest two areas where we still cannot conclude that the work has been done to allow us to responsibly suggest that the Federal Government can now rely on every State's capability. The two I have selected are audit and accounting. The status and work to be done with each is very different. Regarding audit, I think most States have pretty well got their house in order. Regarding accounting, the situation is somewhat different.

I think a hard-nosed examination of State post audit programs would conclude that we are generally in good shape. Further, I think the incentives and pressures of the audit requirements encompassed in the new revenue sharing and counter-cyclical aid programs will cause those few remaining weak States to improve their audit programs.

Thus, as regards audit, I think that State practices can be relied upon, and I think the Federal Government is committed to such reliance. All that remains should be to agree on the detailed mechanisms of such reliance.

I am encouraged about very expeditious progress towards that agreement. The State Auditor Coordinating Council, and through it the NASACT and the NCSL Post Audit Section, the National and Regional Intergovernmental Audit Forums, and individual efforts by GSA, OMB, Treasury, and GAO have all moved us forward. JFMIP is now sponsoring a project which will, hopefully, generate the remaining specific insights and recommendations upon which we can agree and undertake full implementation.

Regarding State accounting, our problem is different. I contended earlier that some States have made amazing progress. Here the States must reach some consensus about State practices. Again, I am able to report encouragement regarding our progress. For three years now at the State level we have been undertaking an intensive effort to create the means to come to grips with the issues of State accounting.

We have now agreed upon an effort involving State auditors, accountants, budget officials, and treasurers, endorsed by the full range of national State governmental organizations and involving fourteen of the largest national accounting firms, to undertake this task. We have two to three years of work ahead of us. I am confident that task will be successfully completed.

I have suggested this morning that at our respective levels of government and in our intergovernmental responsibilities we have faced some difficult problems and in recent years have made progress in which we can take a measure of pride. But the task which lies ahead for governmental financial managers will continue to challenge our commitment and our skill at all levels of government. None of us has all the answers to the problems that confront us, but there are suggestions being made today that we, as professional financial managers in government, are unable to, or cannot be relied upon to, resolve these issues and respond to these challenges. We must work together to prove these critics wrong.

PRESENTATION OF FINANCIAL MANAGEMENT IMPROVEMENT AWARDS
REMARKS OF ELMER B. STAATS
COMPTROLLER GENERAL OF THE UNITED STATES

I am pleased to have an opportunity to participate in this conference and am particularly delighted to have the pleasure of presenting the Financial Management Improvement Awards for 1976. The purpose of these awards is to recognize individuals in Government who have made outstanding contributions to the improvement of financial management in the formulation of policies and programs or in the administration or carrying out of these policies and programs.

Some of the award winners in previous years have been from State and local governments, as well as the Federal Government. The two winners this year are both from the Federal Government but, for the first time, one of them is from the legislative branch.

ALICE M. RIVLIN

In February 1975, Dr. Alice M. Rivlin was appointed the first Director of the Congressional Budget Office which was established by the Budget and Impoundment Control Act of 1974. This new office was charged with providing information with respect to the budget, appropriation bills, authorizing bills, and revenues, to the House and Senate Budget Committees and Appropriations Committees, the House Committee on Ways and Means, the Senate Finance Committee, and other committees of the Congress. It also provides assistance to congressional committees upon request.

The task of organization and staffing of the new office was an important early responsibility of Dr. Rivlin as the first Director. Under her leadership the CBO has become a highly effective professional organization of experts in economics, public finance, and budgeting. The CBO has played an important part in achieving one of the major objectives of the 1974 Act, namely the timely provision of relevant information to aid the Congress in the coordinated review of government financial requirements and resources. Under Alice Rivlin's leadership, economic analysis has become an increasingly effective tool in the budget process. The CBO has provided much needed information and analysis about policy options, without intruding upon the authority of Congress to make decisions.

Many knowledgeable people were frankly skeptical as to how well the new congressional budget process would work. The operation of the new process during the last two years has convinced most people that it can and does work and is working well. While many factors have contributed to this success, Alice Rivlin's leadership of the Congressional Budget Office deserves a great deal of credit.

Alice Rivlin is a graduate of Bryn Mawr College and received her doctorate in economics from Radcliff College. She had two periods of service with the Brookings Institution as an economist and Senior Fellow. She was a co-author of three Brookings' volumes on the Federal budget entitled, "Setting National Priorities" and has written extensively on the Federal budget and economics. From 1966 to 1969, she served with the Department of Health, Education, and Welfare, first as a Deputy Assistant Secretary and then as Assistant Secretary for Planning and Evaluation. During this period she played a major role in implementing the planning, programming, budgeting system in the department and in bringing better program analysis to bear on departmental decisions.

For her contribution in these three capacities, Alice Rivlin does great credit to the Financial Management Improvement Program and I am pleased to present its Annual Award to her at this time.

JOSEPH T. DAVIS

As Assistant Commissioner (Administration) with the Internal Revenue Service, Joseph T. Davis has provided outstanding leadership in the improved management of that agency's resources. His personal and professional commitment to more effective management of the agency's increasingly constrained resources has profoundly influenced the Service's financial planning and budget process. He has brought cost consciousness to all IRS components and activities and has come to be regarded as the Agency's cost reduction catalyst.

Mr. Davis established a system of cost savings incentives through which managers retain for priority needs up to one-half of the savings they generate. He has fostered increased employee participation in cost reduction programs through the incentive awards program. In 1976 tangible benefits from 937 employee suggestions amounted to more than \$2 million and 345 awards were

granted for special achievements which generated more than \$1.3 million in savings. Among the areas in which significant cost reductions have been made are mail management, records disposal, telecommunication services, reports curtailment, better use of space and property, and improved training programs.

An automated budget and accounting system has been designed to more effectively forecast financial requirements, allocate resources and track execution of the financial plan. Other system improvements include an automated inventory control and distribution system, property accounting systems, and a space management information retrieval system.

Cost reduction efforts and financial management system improvements in IRS have generated reductions in overhead expenditures of more than \$20 million per year in the last 2 years alone.

Mr. Davis is a graduate of Saint Anselm's College in Manchester, New Hampshire, and has done graduate work at Georgetown and George Washington Universities. He began his Government service in 1951 with the Navy Department where he served in various personnel and administrative positions. In 1966, Mr. Davis participated in the IRS Executive Selection and Development Program. He has served as Assistant to the District Director in Phoenix and Assistant Regional Commissioner in San Francisco prior to becoming Deputy Assistant Commissioner (Administration) in Washington in 1973. In August 1974, he was appointed to his present position of Assistant Commissioner (Administration).

SUMMARY OF LUNCHEON ADDRESS
DR. REED K. STOREY
TECHNICAL ADVISOR TO THE CHAIRMAN
FINANCIAL ACCOUNTING STANDARDS BOARD

Dr. Storey addressed the attendees on the Financial Accounting Standards Board and its Conceptual Framework Project. The FASB, created in 1973 to succeed the Accounting Principles Board, is the rule-making body for the accounting profession.

The Conceptual Framework Project is a major continuing effort that will set the course for financial accounting and reporting for the future. It is aimed at developing a coherent system of interrelated objectives for the financial community that can lead to consistent standards and that prescribe the nature, function and limits of financial accounting and financial reporting. The project is being carried out in several phases, two of which are currently under way.

One phase involves consideration of the objectives of financial statements, about which the FASB has now reached tentative conclusions. The other is concerned specifically with definition and measurement of the elements of financial statements--assets, liabilities, owners' equity or capital, earnings, revenues, expenses, gains, and losses. Other phases are anticipated that will be concerned with matters such as form and content of financial statements, allocation (including depreciation and amortization), and certain aspects of revenue recognition.

In December 1976, two documents were published as part of the Conceptual Framework Project, one relating to the objectives of financial statements and the other dealing with the elements of financial statements and their measurement. Titles of the two documents are:

- "Tentative Conclusions on Objectives of Financial Statements of Business Enterprises."
- FASB Discussion Memorandum--"Conceptual Framework for Financial Accounting and Reporting: Elements of Financial Statements and Their Measurement."

A third document: "Scope and Implementation of the Conceptual Framework Project," was produced for persons interested in a capsulated view of the other two documents.

The "Tentative Conclusions" document defines three tentative conclusions about the objectives of financial statements of business enterprises:

1. Financial statements of business enterprises should provide information, within the limits of financial accounting, that is useful to present and potential investors and creditors in making rational investment and credit decisions. Financial statements should be comprehensible to investors and creditors who have a reasonable understanding of business and economic activities and financial accounting and who are willing to spend time and effort needed to study financial statements.
2. Financial statements of business enterprises should provide information that helps investors and creditors assess the prospects of receiving cash from dividends or interest and from proceeds from the sale, redemption, or maturity of securities or loans. Those prospects are affected (1) by an enterprise's ability to obtain enough cash through its earning and financing activities to meet its obligations when due and its other cash operating needs, to reinvest in earning resources and activities, and to pay cash dividends and interest and (2) by perceptions of investors and creditors generally about that ability, which affect market prices of the enterprise's securities relative to those of other enterprises. Thus, financial accounting and financial statements should provide information that helps investors and creditors assess the enterprise's prospects of obtaining net cash inflows through its earning and financing activities.
3. Financial statements of a business enterprise should provide information about the economic resources of an enterprise, which are sources of prospective cash inflows to the enterprise, and which are causes of prospective cash outflows from the enterprise; and its earnings, which are the financial results of its operations and

other events and conditions that affect the enterprise. Since that information is useful to investors and creditors in assessing an enterprise's ability to pay cash dividends and interest and to settle obligations when they mature, it should be the focus of financial accounting and financial statements.

Unlike the "Tentative Conclusions", the Discussion Memorandum contains no conclusions of the Board. It is instead an analysis of issues related to defining and measuring the elements of financial statements--assets, liabilities, capital, revenues, expenses, etc. A "bridge" chapter discusses the relation of the Discussion Memorandum to the Board's tentative conclusions on objectives of financial statements.

The remainder of the Discussion Memorandum is divided into three parts. Part I, comprising five chapters, is concerned with defining the elements of financial statements. Part II, consisting of one chapter, discusses the qualitative characteristics of financial information (for example, relevance, objectivity, comparability). Part III, comprising three chapters, is concerned with the attributes (for example, historical cost, replacement cost, current selling price) of the elements of financial statements that should be measured to provide the most relevant and reliable information in financial statements.

The Conceptual Framework Project will lead to definitive pronouncements on which the Financial Accounting Standards Board intends to rely in establishing financial accounting and reporting standards. Though the framework cannot and should not be made so detailed as to provide automatically an accounting answer to a set of financial facts, it will determine bounds for judgment in preparing financial statements. The framework should lead to increased public confidence in financial statements and aid in preventing proliferation of accounting methods.

WORKSHOP I

CASH MANAGEMENT

Chairman: Lloyd Morgan, Assistant Commissioner,
Banking and Cash Management,
Bureau of Government Financial Operations
Department of the Treasury

Panelists: George J. Anthony, Assistant Manager
General Accounting Office (New York)

James R. Glassco, Jr., Treasurer
U.S. Postal Service

Daniel McGrath, Acting Director
Special Financing Staff
Bureau of Government Financial Operations
Department of the Treasury

Interest in the area of cash management is ever increasing. In the United States Budget for FY 1977, it is estimated that 11 cents of every dollar obtained is acquired through borrowing, and 8 cents of every dollar spent goes for interest. In short, the U.S. Government is borrowing 11 cents and paying 8 cents in interest.

At this workshop representatives from three organizations discussed their efforts towards improving cash management.

Mr. Glassco of the U.S. Postal Service explained how Postal Service revenues are collected, how cash is managed on a daily basis, and how costs are monitored. With an annual cash flow of approximately \$17.8 billion and some 40,000 post offices, stations, and branches, the Postal Service was able to accelerate the availability of its revenues by reducing the number of its bank accounts from 90,000 to 9,500 and by using wire transfers initiated by concentration banks. Daily revenues are deposited into accounts at depository banks. The next day all receipts are transferred to 21 concentration banks, which on that same day wire transfer the funds to the Federal Reserve Bank (FRB) of New York. Hence field collections of checks and cash are turned into funds at the New York FRB in two days.

In addition to collecting its revenues seven days earlier, the Postal Service is also able to manage its

cash more effectively by receiving daily reports on expected revenues and projected disbursements, which enable the Treasurer to know what funds will be available for investment or required for settlement. With the aid of its computerized cash forecasts and history file, the Postal Service ensures that its payments are timely and its excess funds are fully invested. To monitor the costs involved in collecting revenues, the Postal Service used a break-even analysis to determine the minimum deposit for which use of the wire transfer is justified. It has also developed various options for compensating banks for services rendered while minimizing its overall costs.

Mr. McGrath of the Department of the Treasury gave a brief presentation of the letter-of-credit method, discussing its historical background, refinements, and current developments. In the early 1960's, audits had revealed that substantial amounts of cash were being withdrawn from the U.S. Treasury long before the funds were actually needed by the recipient organizations (grantees). Since these premature disbursements led to substantial and unnecessary borrowings and increases in interest costs to the Treasury, the letter-of-credit method was recommended by the JFMIP to slow the rate of cash withdrawals from the Treasury while providing recipient organizations with enough cash to carry out federally funded programs. In 1964 the letter-of-credit Federal Reserve Bank System was established, enabling the recipient organization to fund its disbursements and drawdown on a letter of credit through a commercial bank, which in turn received its funds through the Federal Reserve Bank System. Various refinements were required in these advance funding procedures since effective control of the FRB letter-of-credit method relies upon the good faith of the recipient organization and the monitoring efforts of the Federal program agency. The letter-of-credit method became mandatory for Federal program agencies in those cases where there is a continuing relationship with the grantee for at least one year involving annual advances of at least \$250,000. This method was also made available for use by Federal program agencies for funding loan programs which carry interest rates that are lower than the Treasury borrowing rates.

The letter-of-credit method is now used by almost every Federal agency administering Federal grant programs. Disbursements under this method have grown from \$1.5 billion in the 1960's to over \$63 billion in FY 1976. As of June 30, 1976, there were over 8,000 active letters of credit. It is conservatively estimated that annual recurring interest savings to the Treasury as a result of the use of the letter-of-credit method have reached approximately \$227 million.

After explaining various letter-of-credit techniques such as single letter of credit, delay of drawdown, and checks paid, Mr. McGrath went on to describe one of the most promising concepts being supported by Treasury--the Letter of Credit-Treasury Regional Disbursing Office System (RDO System). Under the RDO System, the letters of credit are maintained at the Treasury Disbursing Offices and the drawdowns are handled through the Treasury Disbursing Offices for payment by Treasury check instead of through the Federal Reserve Banks. The basic differences between the RDO and the FRB Systems are the source of payment, the data required, and the procedures available to the Federal agencies to stop excessive drawdowns. Treasury's evaluation of the RDO System indicates it is an effective tool for minimizing premature withdrawals by recipients and it gives the Federal agencies a better tool for controlling advances and monitoring their recipients. Treasury regulations are currently being revised to mandate the RDO letter-of-credit system for most recipient organizations, and to lower the criteria where the letter-of-credit method shall be used from \$250,000 to \$120,000.

Mr. Anthony of the General Accounting Office commented on a study which is being performed on the payments policy of the Federal Government. Because of many late payments by the Government, congressional interest, and the significant impact of Federal purchases, a study is being undertaken to determine, among other things, when payment is due, if Federal payments are untimely, why, and what could be done. By sampling various payment centers, invoices, and contractors, it was found that there is widespread disagreement concerning when payment is due. Assuming payments not received within 30 days of the invoice date to be late, 30 percent of Federal payments are late; however, many Federal payments are also early. Late receiving of reports appeared to be a major cause for late payments, but other causes related to payment center and delivery problems. To alleviate the problem of untimely payments, it was suggested that a general payment standard be established, the need for receiving reports be reduced, discount policies be strengthened, and certified invoices and imprest funds be used more frequently.

It is in the area of timing of receipts and disbursements that Federal financial managers can have the greatest impact. However, in accelerating collections and delaying disbursements, managers must also strive to reach an equitable solution.

WORKSHOP II

FEDERAL CONSOLIDATED FINANCIAL STATEMENTS

Chairman: Gerald Murphy, Deputy Commissioner
Bureau of Government Financial Operations
Department of the Treasury

Panelists: Nathan Cutler, Executive Vice-President
Association of Government Accountants

Jacquelyn Mullins, Supervisory Systems Accountant
Financial and General Management
Studies Division
General Accounting Office

Michael T. Smokovich, Committee Manager
Advisory Committee on Federal
Consolidated Financial Statements
Bureau of Government Financial Operations
Department of the Treasury

The workshop focused on the major thrust of recent developments in Federal financial reporting which is towards the preparation of consolidated financial statements on an accrual basis.

Michael Smokovich, Committee Manager of the Advisory Committee on Federal Consolidated Financial Statements, outlined the events leading up to the establishment of the Advisory Committee and the publication of a prototype consolidated financial statement for the Federal Government by the Department of the Treasury.

Mr. Smokovich pointed out that the preparation of a Federal consolidated financial statement prepared on an accrual basis was not an entirely new concept. However, the idea has received renewed interest because current economic conditions and the extensive use of deficit financing by the Federal Government have generated a need for better overall financial reports that show clearly, for the benefit of Congress and the public, the major aspects of the Federal Government's financial positions and operations. Traditional government financial reports seldom provide a simple overview of what a government owns and what it owes or an explanation of how it got where it is. They concentrate primarily on the matter of compliance with specific legislative authorizations. Compliance reporting is an essential function of

governmental accounting but events of the last few years, particularly the rising and seemingly uncontrollable Federal deficits and the financial crises in major cities and states, point to the need for a new perspective--one that looks at government as a total financial entity and describes its financial condition in plain language and plain accounting.

Task groups were formed to research these issue areas and report their findings to the Advisory Committee. Jacquelyn K. Mullins of the General Accounting Office, who participated in several of the task groups, briefly discussed the status of each of the issue areas and highlighted the types of problems encountered by the task groups by focusing on two issue areas, asset valuation and reporting pension fund liability. A slide presentation on each of these areas illustrated the methodology used by the task groups in arriving at their recommendations to the Advisory Committee.

Nathan Cutler, Executive Vice-President of the Association of Government Accountants and member of the Advisory Committee, discussed the role of the Advisory Committee in the development of Federal consolidated financial statements. Mr. Cutler emphasized the complexity of the questions which the Committee has been asked to comment on and the diversity of opinions surrounding these questions.

After the three panel members had spoken, workshop participants questioned the panel on various aspects of the development and preparation of the consolidated financial statements. The majority of the questions focused on implementation problems such as whether additional reporting requirements would be imposed on Federal agencies as a result of the preparation of Federal consolidated financial statements.

WORKSHOP III

INTERGOVERNMENTAL AUDITING

Chairman: William A. Broadus, Jr., Assistant Director
Financial and General Management Studies D
Division
General Accounting Office

Panelists: Frank Greathouse, Director of State Audit
State of Tennessee

Malcolm Stringer, Director
Office of Audit
Environmental Protection Agency

The major emphasis of the workshop centered around problems confronting intergovernmental auditing and how the State Auditor of Tennessee and the auditor of EPA have faced some of these problems.

There was agreement among the panelists that there was a need for more improvement in coordination and cooperation among governmental audit organizations. The variations by which Federal funds moved to the final recipient as well as the various ways these funds are audited contribute to the problems faced in intergovernmental audit coordination and cooperation.

Some of the major problems discussed were:

- Need for safeguards to maintain auditor independence.
- Need for a system to give advanced notice of grant awards to assist in scheduling audits.
- Varied audit requirements, guidelines, and report formats among Federal agencies.
- Need for audit cost reimbursement and for the procedure to provide for sustain funding and timely reimbursement.

There was general consensus that solutions to many of these problems are not yet in hand but that progress is being made. A great deal of credit was given to the intergovernmental audit forums which have made it possible for the government auditors from all levels to get together and jointly work out these mutual problems. It was also felt that the current JFMIP Audit Improvement Project

would help bring about solutions to many of the problems discussed.

The panelists discussed how Tennessee and EPA had been successful in working out audit arrangements whereby Tennessee could satisfy the audit requirements of EPA and likewise could receive timely and adequate reimbursement for the audit costs incurred. The EPA has solicited the assistance of State auditors to satisfy their audit needs and to comply with Financial Management Circular 73-2, which requires that the Federal audit agencies rely to the maximum extent possible on State and local auditors to audit federally assisted programs. Although the responses from State auditors were not as favorable as EPA would have liked, there were several State auditors that entered into agreements with the EPA to audit federally assisted funds. The reasons State auditors gave most often for the unfavorable responses to EPA were that they had insufficient staff, they previously had some bad experiences with Federal agencies, and it was difficult to get direct reimbursement to State audit agencies for the audit of federally assisted funds. The EPA enters into contractual agreements with the State audit agencies whereby the EPA Office of Audit directly reimburses the State auditors or organizations for work performed. Presently EPA is contracting with some six State audit organizations to audit EPA grant funds. EPA is presently working with the State of Tennessee under this arrangement.

It appeared to be the general consensus of the panelists as well as the audience that many of the problems discussed are directly related to audit coordination and cooperation, and that although many problems remain to be solved, there is an effort being made--and progress as well--to overcome some of them; organizations such as the intergovernmental audit forums have been instrumental in helping to solve many of these problems.

WORKSHOP IV
ZERO-BASE BUDGETING

Chairman: George H. Strauss, Chief
Resources Systems Branch
Budget Review Division
Office of Management and Budget

Panelists: Arthur D. Kallen, Director
Office of Budget and Program Analysis
Department of the Treasury

Howard Messner, Assistant Director
Management Programs
Congressional Budget Office

Benson J. Simon, Senior Analyst
Committee on Budget
U.S. House of Representatives

Joel E. Smith, Captain
Office of the Comptroller
Department of the Navy

The workshop served as a useful and informative follow-on to the comments on zero-base budgeting in Dale McOmber's morning speech. Mr. Strauss from OMB reinforced the morning's remarks with finer detail on the implementation process. However, he noted that much remained to be resolved within OMB and that significant changes to the process could still occur. As developed at that time, it was OMB's intention to issue guidance to the agencies around the middle of March, with possibly more to be issued with the allowance letter and the revised OMB Circular A-11 which OMB will attempt to transmit earlier this year in June. Mr. Strauss stated that OMB's thinking at the time was that the actual zero-base work would be done at the agency level, with only the results of the analysis contained in the budget submission, at the functional account level.

Benson Simon and Howard Messner spoke on the involvement of the legislative branch with the ZBB and "sunset" processes. Mr. Messner spoke on the congressionally-mandated ZBB effort currently underway at the Consumer Product Safety Commission. Mr. Kallen and Captain Smith discussed experiences with ZBB in the Bureau of the Mint and the Navy's Operations and

Maintenance program, and the difficulties they have encountered. Some of the specific problems which have been encountered at the CPSC, Bureau of the Mint, and Navy are:

- What is the basis for the minimal or "survival" level? Is it mandated 75 percent - 85 percent of of the current program, or is it left to the judgment of program officials?
- How are decision packages established which are both functionally and authoritatively responsive?
- How are field operations to be considered?
- How can the paperwork of the process be controlled?

The session ended after an extensive question and answer session, at which the speakers concurred that there were a great deal of problems in implementing ZBB at even a single organization or program level, much less government-wide, and that considerable effort will be required by government financial managers in implementing ZBB.